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Dealing with Change

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Over the life of a typical PPP contract—10 to 30 years—developments will occur that could not have been predicted when the contract was signed. It is also likely that the parties will dispute contract interpretation, or whether both parties have been performing as agreed. In some cases, these disputes may result in early termination of the contract. These risks cannot be avoided—but they can be managed.

Some general guidance material that is available on dealing with change in PPPs is:

- The **United Kingdom's National Audit Office publication** on managing the PFI relationship (NAO 2001), which emphasizes the need for public authorities to address the question of contract management early in the project preparation and the presence of appropriate skills within the public authority. It also highlights the importance of an open and cooperative attitude.
- A shorter overview on similar topics is provided in **Quick's article on managing PPP contracts** (Quick 2003), which also adds an Australian perspective.
- **UNESCAP's PPP guidebook** (UNESCAP 2011, Chapter 6) offers an overview of contract management intended for developing countries. It focuses on institutional arrangements for contract management, and mechanisms for dispute resolution.

These materials do not provide the detailed guidance that would benefit government officials. Therefore, this section also provides examples of where these issues have come up, and ways in which they have been handled, from which practitioners can draw lessons. These change situations can usefully be discussed in four categories:

- Planned reviews and adjustments
- Renegotiations
- Disputes
- Contract expiry or termination

Planned reviews and adjustments

Well-structured PPP contracts build in adjustment mechanisms for dealing with the more common types of unexpected change, as described in Adjustment Mechanisms. In addition to being aware of, and following, the rules in the contract, contract managers need to make sure required institutional elements are in place, as described in the **EPEC Guide to Guidance** (EPEC 2011b, 37–38). For example, this could include ensuring expert panels have been identified and are qualified, and all steps are clear to all parties involved.

Renegotiation or contract variations

Many PPP contracts are renegotiated, often early, as described by **Guasch in his book on renegotiation in PPPs** (Guasch 2004). *Renegotiation* refers to changes in the contractual provisions, rather than through an adjustment mechanism provided for in the contract. Renegotiation is something to avoid where possible. Good use of adjustment provisions, as outlined above, can obviate the need for renegotiation.

Still, renegotiations will from time to time be needed, and governments will benefit from understanding good policy for conducting them. **Partnerships Victoria's Contract Management Manual** (VIC 2003, Section 7.3) describes the understanding that public parties should have of the private party's financial health, as well as project performance. While not focused specifically on renegotiation, having this information and understanding will benefit government as it considers decisions that could result in renegotiation.

Some examples of renegotiations that may offer some insights into good practice, and which have been documented include:

- **The Melbourne Tram and Train concessions**. When these concessions were in financial difficulty, the government decided to renegotiate rather than terminate, as this was expected to provide better value for money—see **Ehrhardt and Irwin** (Ehrhardt and Irwin 2004). To provide transparency and quality assurance on the process, the government announced early in the process that, after the negotiations were complete, they would be subject to an ex-post value for money analysis. This analysis was published as an **Auditor General's report** (VIC 2005), which describes the renegotiation process and results.
- **The United Kingdom National Air Traffic Services (NATS) PPP**, also described by **Ehrhardt and Irwin** (Ehrhardt and Irwin 2004), was a more controversial restructuring. The PPP Company faced falling revenue because of a sharp downturn in air travel after the 9/11 terrorist attacks in the United States. The company looked certain to default on its debt. The Board of the Civil Aviation Authority (the public party to the PPP) was split. The Board member directly responsible for the contract insisted the government should not renegotiate, stating the solution was a private sector financial restructuring, in which the lenders to the company would bear some of the losses. The majority of the Board disagreed, however, and instead agreed to change the terms of the contract as part of a package deal that also involved some debt restructuring.

In contrast to the United Kingdom NATS experience, the **government of New South Wales** managed to avoid renegotiating the PPP contract for a highway tunnel under Sydney's central business district when it went into financial distress. Instead, the matter was resolved entirely through a private sector financial restructuring. **Johnston and Gudergan** subsequently reviewed the experience to draw lessons for PPP governance (Johnston and Gudergan 2007). An **OECD paper on PPP renegotiation in the US** (Gifford et al. 2014) presents renegotiation cases in the United States and shows how they are linked to opportunism and may affect infrastructure development.

Road contract renegotiations in **Portugal** and **Spain**, during the recent economic and financial crisis, present an interesting case of renegotiation under fiscal stress—but lessons have not yet been reported. The British National Audit Office (NAO 2013b) reported on similar renegotiations for reducing service levels and obtaining project savings.

Disputes

Contractual disputes arise when one party believes the other has not done something it was contractually obliged to do, but the other party disagrees as to what its obligations were, or what should be done to remedy the situation.

The **Partnerships Victoria *Contract Management Guide*** (VIC 2003, Section 8.3) includes a section on dispute resolution. A helpful distinction is made between issues and disputes, as set out in Distinction between Service Delivery Issues and Disputes.

Distinction between Service Delivery Issues and Disputes

SERVICE DELIVERY ISSUES	DISPUTES

Need not involve any difference of opinion or position between the parties	Involves a difference of opinion or position between the parties (by definition)
Interruption or other disturbance to service delivery	Need not involve any interruption or other disturbance to service delivery
May trigger an abatement of service fees, or other remedies	Generally, will not in themselves trigger an abatement of service fees

Source: (VIC 2003)

The **Partnerships Victoria Contract Management Guide** also contains sample templates for specifying how issues may be escalated (VIC 2003, Template M) and disputes resolved (VIC 2003, Template N). The practical advice offered focuses on the desirability of speedy informal resolution of disputes, understanding the other side's position, and avoiding inappropriate dispute processes, since these can damage the long-term relationship.

Focusing on finding practical solutions quickly, and taking into account the other side's position, often yields positive outcomes when trying to resolve disputes. However, countries do not necessarily find it appropriate to seek resolution through informal mechanisms. For a variety of reasons, they often prefer to follow the formal steps set out in the contract. Whichever route they choose to follow, they should seek to reach a practical solution.

There are numerous examples of the costs that governments end up bearing because of choosing inappropriate dispute resolution methods. For example, the government of **Tanzania** was justifiably dissatisfied with the performance of the private firm operating the water system in Dar es Salaam. The PPP contract provided a dispute resolution mechanism under which the government could very likely have achieved the redress it sought, and won damages from the contractor. However, as described in a review of the dispute case (Triantafilou 2009, 6):

"While the contractual relationship was headed inevitably towards dissolution, Tanzanian Government officials, motivated by electoral concerns, among others, took a series of drastic measures that went far beyond the contractually mandated process for termination of the Project Contracts. In May 2005, Tanzanian Government officials, causing public furor, repudiated unilaterally and rather publicly the lease agreement with City Water while calling on the performance bond posted by BGT, reinstated the previously waived VAT on purchases by City Water, repossessed forcibly the assets previously leased to City Water, and deported City Water's BGT-appointed management."

Cases of PPP disputes and how they have been handled are available on the website of the International Centre for the Settlement of Investment Disputes (ICSID, a part of the World Bank Group)—see International Centre for Settlement of Investment Disputes. In July 2010, an ICSID arbitration tribunal ruled that the Argentinian government unfairly refused to allow the private concessionaires to raise tariffs during the period after the devaluation of the Argentine peso in 2001 and awarded damages to the private companies—see When PPPs fail—The case of the 1993 water concession in Buenos Aires on this conflict.

Overly also provides a critical review of the use of international arbitration, in a range of PPP and similar cases (Overly 2010). Many of these cases suggest that governments can minimize the costs of disputes to the public sector if they:

- Act quickly when problems start to arise
- Have teams with the right skills and appropriate levels of decision-making authority working on resolving the issue
- Follow processes set out in the contract
- Look for win-win solutions, considering the broader public interest and the private parties' options

Resolve the issues at the lowest level possible and only escalate if they are not resolved

Related Content

- **INTRODUCTION**
- **PPP BASICS: WHAT AND WHY**
- **ESTABLISHING THE PPP FRAMEWORK**
- **PPP CYCLE**
- **Identifying PPP Projects**
- **Appraising Potential PPP Projects**
- **Structuring PPP Projects**
- **Designing PPP Contracts**
- **Managing PPP Transactions**
- **Managing PPP Contracts**
- **Dealing with Unsolicited Proposals**
- **Key References - PPP Cycle**

Additional Resources

- Pandemics and PPPs
- Managing Technological Change

Find in pdf at PPP Reference Guide - PPP Cycle or visit the PPP Online Reference Guide section to find out more.

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